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XRAY - Q1 2010 DENTSPLY International Inc. Earnings Conference Call

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PRESENTATION

Operator

Good day, and welcome to the DENTSPLY International 2010 first quarter earnings conference. Today's call is being recorded. At this time I'd like to turn the conference over to Mr. Bret Wise, Chairman and CEO. Please go ahead, sir.

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

Thank you, Christian. Good morning, everyone, and thank you for joining us on our first quarter call. This is Bret Wise, Chairman and CEO. And also with us today are Chris Clark, our President and COO, and Bill Jellison, our Senior Vice-President and CFO. Each of us will have some prepared remarks this morning and then, following our prepared remarks, we'll be glad to answer any questions you may have. Before we get started, it's important to note that this call will include some forward-looking statements and those are subject to risks and uncertainties that are described in our SEC filings, including our most recent report on our annual report on Form 10-K, as well as our quarterly reports, press releases, and other filings. The Company undertakes no obligation to update or revise the forward-looking statements to reflect events or circumstances that may arise after the date of this call. And as usual, a recording of this conference call in its entirety will be available on our website.

This morning we announced our results for the first quarter 2010 and we're pleased to report a continued acceleration in growth following what we believe was a bottoming of the dental markets mid-last year. As we expected and commented on in our year end call, we expect 2010 to start slow, probably with a gradual recovery that varies widely by geographic region. This, frankly in fact, is what we have seen and, although there are promising signs in certain geographies or product categories, it is



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apparent that we're still in the early stages of recovery of many of the dental markets. It's important to keep in mind that the dental market is usually a bit of a trailing indicator, both going into and also coming out of recessions, as our markets tend to lag the overall economy just a bit. For the first quarter 2010, our overall growth was 7.7%, aided by internal growth and also benefiting from a weaker dollar on a year-over-year basis. Sales without precious metal increased 6.8% and that was driven by internal growth of 2.5%, acquisition growth of 0.2%, giving us constant currency growth of 2.7%. And it was also aided by currency, which added 4.1% in the first quarter. The internal growth by geography was plus 0.9% growth in the US, 2.4% growth in Europe, and 6% growth in the rest of the world category.

On a product category basis, we continued to see some acceleration in the chair-side consumables, which grew mid single-digits. The specialty projects -- products as a category continued low single-digit growth and that is consistent really with what we saw throughout 2009. And the lab category contracted low single-digits. The continued improvement in the chair-side consumables, I think, is encouraging, as we would expect those products that are used every day in the operatorily really to be the first to recover and begin to grow. This is an area, of course, where we had a favorable comparison last year, particularly outside of the US, with some dealer destocking in the base. However, despite that, we view the growth this quarter as encouraging and reflective of early signs of more normal growth returning to this market, although slowly. In the specialties, I would say there is not a robust recovery at this point. However, as we stated before, these are in some ways the most discretionary and most expensive procedures.

It's also important to realize that we had internal growth in this category in each quarter last year, so for us we're, not going up against an easy base period at this point. Despite that, it's comforting to see that these products are continuing to grow, albeit slowly, at this point. And, although the prosthetics products remain negative in the quarter, the degree of such was much less than we had seen in prior quarters. So, perhaps this is an area that's also turning the corner or getting close to turning the corner at this point. Overall, I would say that there is some reasonably good signs on many fronts in the dental market both on a geographic basis and a product category basis. From an earnings perspective, we saw our gross margins improve sequentially by 200 basis points, compared to the fourth quarter of 2009. You might recall from our year end call that we had expected to see some sequential improvement in our margins. And, although we also commented that there would likely be some year-over-year declines remaining in the first quarter, and that was due to both a tough comparison coming out of the first quarter last year, some adverse currency impacts that will be affecting us this year, and also lower plant absorption as we had much tighter control of inventories in the first quarter of 2010 versus what happened in 2009. And that's essentially what happened.

We had a year-over-year decline in our margins of 40 basis points, but a sequential improvement in our gross margins over Q4 2009 of 200 basis points. I think it's also important to note that at 56.7% gross margins in Q1 of 2010, we are starting out a full 90 basis points above the full-year 2009 gross margins. So, overall on a GAAP basis, earnings were essentially flat with the prior year in the first quarter of 2010, and on a non-GAAP basis at \$0.44 a share, increased 2.3% over the first quarter of 2009. In total, I'd say we're starting out the year about as we had anticipated on a pure operating basis, although our currency assumptions were for a much stronger Euro exchange rate at this point. Also during the quarter, we repurchased approximately 1.2 million shares under our prior authorization, and as you probably saw, we announced earlier that our Board of Directors increased our authorization by 5 million shares in late March. We did complete two small acquisitions in the quarter, both in Europe, and we signed LOIs on two other small transactions, which we would expect to close in Q2 or Q3. In addition, we continue to be active in discussions with other companies for collaborations or acquisitions and are hopeful that we can see some continued acceleration in this activity as we move forward.

Looking forward, we're pleased to be off to a good start and still expect a gradual recovery throughout 2010. We remain comfortable with our earlier guidance of low single-digit internal growth for the full year. From a total gross standpoint, we have seen the Euro continue to weaken, and at current rates, it would be a slight negative in Q2 and would be much more of a headwind in Q3 and Q4 if those rates don't recover somewhat. We are confirming our earnings guidance at \$1.90 to \$2 per share for all of 2010. However, this can also be influenced by the strength of the dollar. For the full year, our guidance continues to be based on a Euro of \$1.39 and, although there are still many variables to manage, a stronger dollar would tend to push us towards the lower end of that guidance, and a weaker dollar would tend to push us towards the higher end of that guidance.



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That concludes my prepared remarks. I'd like to turn the call over now to Chris Clark, who's going to give you an update on our new products and our innovation efforts.

Chris Clark - *DENTSPLY International Inc. - President & COO*

Thank you, Brett. Good morning, everyone. I'd like to take a few moments and give you some additional insights into some of our key innovation efforts, as well as our recent Global Implant Symposium that was held in Barcelona last month. Innovation continues to be a key growth platform for us. Since the beginning of the year, we have introduced nine new products. Highlighting just a few of these this morning, in the prosthetics area we introduced the new Ceramco iC Integrated ceramic system. This is a fully integrated universal porcelain system that allows -- that offers a complete range of aesthetic shades and also improves strength. This allows dental laboratories to replicate the optical characteristics of natural dentition or natural teeth, while reducing processing steps and minimizing their inventory investment. Further, the Ceramco iC system can be fabricated across a wide range of platforms, helping our lab customers to stay competitive on all ceramic, porcelain fused-to-metal, and also pressed to metal restorations.

In the endodontics area, we introduced the new Exmark EZ cordless endodontic handpiece to the US market. This light-weight, simple to use endodontic motor features a comfortable and well balanced cordless handpiece that adds a slim head that can be adjusted to allow for an improved field of vision and also better access, which are both critical features for dentists that are performing root canal procedures. We also continue to gain momentum on new products that we introduced last year.

On previous calls, I think I've mentioned our August 2009 introduction of the SureFil SDR Posterior Bulk Fill Flowable composite. This product allows for excellent cavity adaptation and also bulk placements up to four millimeters in depth, and results in up to 30% less placement time for the dentist. Importantly, this unique chemistry employs a new stress decreasing resin system that addresses one of the primary causes of procedural failure for composites, namely stress accumulation during curing. In the US, we've achieved more than \$2.5 million in retail sales in the first eight months since we've introduced the product. And we've achieved over \$2 million in wholesale sales in Europe since we introduced the product there in January. Globally, over 21,000 dentists have tried the product, and over 11,000 of those are new customers to DENTSPLY in the category of dental composites. Customer feedback has been just exceptionally positive and we're enjoying very positive reviews from the various product rating agencies as well.

Looking forward, in the orthodontics area we've announced the upcoming introduction of our MTM, or minor tooth movement Clear Aligner, which is a minor tooth movement system that uses software and digital scanning technology to deliver a series of clear custom fit aligners that progressively move teeth into the prescribed treatment plan position. This system utilizes our internal aligner service center, which -- with dentists and orthodontists sending us an impression or patient model, from which we would then fabricate multiple aligners for that specific patient. We will be showing the MTM Clear Aligner product at the upcoming American Association of Orthodontics meeting that is this weekend in Washington, D.C. And we'll begin shipments after we receive final regulatory clearance.

Finally, I'd like to touch briefly on our Global Implant Symposium that we held last month in Barcelona, Spain. We were extremely pleased with this event, as we had over 2,500 attendees from over 67 different countries. The symposium included a comprehensive scientific program that was led by almost 100 international lecturers and discussed a wide range of implant topics. It also provided us a very strong platform to showcase our range of implant products, including the Ankylos implant system, which we continue to believe is one of the fastest growing implant lines globally. I'd like to now turn the call over to Bill Jellison, our Chief Financial Officer, to discuss the first quarter financial results in greater detail.

Bill Jellison - *DENTSPLY International Inc. - Senior Vice President & CFO*

Thanks, Chris. Good morning, everyone. Net sales for the first quarter of 2010 increased by 7.7% in total, an increase by 6.8% excluding precious metals. The sales increase ex-precious metals for the quarter included a constant currency increase of 2.7%,



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which includes a 2.5% increase from internal growth, and a 0.2% increase from acquisitions. The quarter was also positively impacted 4.1% from foreign exchange translation, as the dollar weakened against most currencies from last year's first quarter. The geographic mix of sales ex-precious metals in the first quarter of 2010 included the US at 37.4%, Europe represented 42.7%, and the rest of world was 19.9% of sales. Gross profit margins as a percent of sales ex-precious metals content in the first quarter of 2010 were 56.7%, compared to 57.1% for the first quarter of 2009. The rate was negatively impacted in the quarter compared to the same period last year due to negative product mix within the product lines, foreign exchange transactional impacts, and also lower plant cost absorption compared to the prior period, when we had significantly -- significant inventory build, which was offset, somewhat, by price increases. These negative impacts were partially offset by the higher rolloff of acquisition inventory step-up costs in 2009.

Although margins were lower than in the first quarter last year, they improved 2 full percentage points sequentially as price, mix, FX, and manufacturing costs all improved. SG&A expenses were \$188 million, or 37.8% of sales ex-precious metals in the first quarter of 2010, versus 38.2% in the prior year's first quarter, a 40 basis point improvement. These expenses were lower as a percent of sales, primarily due to reductions that were made during 2009, partially offset by additional investments made to strengthen our future growth prospects, as well as from the normal resetting of some of our variable costs, such as commissions, rebates, and bonuses. Of the \$10 million increase in SG&A, \$8 million is from the impact of FX movement and acquisitions. Operational margins for the quarter were 16.4%, compared to 17% in the first quarter of last year. Operating margins based on sales excluding precious metals were 18%, compared to 18.5% last year in the same period. Operating margins based on sales excluding precious metals, for comparative purposes, excluding recent acquisition-related activities and restructuring and other costs in both periods, would have been 19% in the first quarter of 2010, and 19.4% in the first quarter of 2009.

Net interest and other expense in the first quarter was \$5.9 million, compared to net interest and other expense of \$5.1 million last year in the first quarter. The increase in expense in this area resulted primarily from higher net interest expense, which reflects lower returns on our cash balances. The corporate tax rate in the quarter of approximately 26% is relatively consistent with the first quarter of 2009. We expect this to be reasonable assumption for an operational tax rate for 2010. Net income attributable to DENTSPLY International for the first quarter of 2010 was \$61.8 million, or \$0.41 per diluted share, compared to \$0.41 per diluted share in the first quarter of 2009. Net income attributable to DENTSPLY International in the first quarter on an adjusted non-GAAP basis, excluding restructuring and other costs, recent acquisition related activities, and income tax related adjustments was \$65.5 million or \$0.44 per diluted share in 2010, compared to \$64.1 million or \$0.43 per diluted share in the first quarter of 2009, which is a 2.3% improvement in EPS.

Cash flow from operating activities in the first quarter of 2010 was approximately \$37 million, compared to \$11 million in the same period last year. The cash flow in the first quarter of 2010 was higher than last year due primarily to an increase in accrued liabilities and accounts payable associated with various variable cost categories, and less inventory build in the first quarter of this year compared to last year. Capital expenditures were \$8 million in the first quarter, with depreciation and amortization at \$17.8 million in the period. Inventory days were 103 at the end of the first quarter of 2010, compared to 115 at the end of the first quarter last year, and 99 days at the end of 2009. Receivable days were 59 days at the end of the first quarter in 2010, compared to 58 days at the end of the first quarter in 2009, and 55 days at the end of 2009. We believe our accounts receivables remain in good shape and continue to be a focus of our team. At the end of the first quarter of 2010, we had \$405 million in cash and short-term investments. Total debt was \$477 million at the end of the first quarter. During the first quarter, we have also repurchased \$41 million or 1.2 million shares at an average price of approximately \$33.59 per share.

Based on the Company's recent increase in its authorization, which allows us to maintain up to 22 million shares of treasury stock, we still have approximately 5.5 million shares available for repurchase, and would expect some continued repurchase activity this year. Finally, as Brett noted, we are reconfirming our full-year guidance for diluted earnings per share of \$1.90 to \$2, excluding the impact of restructuring and other costs, acquisition-related activities, and one-time adjustments. The mid-range of this guidance is based on an average dollar rate compared to the Euro of approximately \$1.36 to \$1.40, which is a stronger Euro than exists today. That concludes our prepared remarks. Thanks for your support and we'd be glad to answer any questions that you may have at this time.



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QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

And we'll pause for a moment to assemble our queue. We'll go first to John Kreger with William Blair.

John Kreger - William Blair - Analyst

Hi, thanks very much. Bill, just a quick follow-up on that last remark you made. If you look at the Euro exchange rates where they are now, what would you estimate would be the earnings that you absorbed, if those exchange rates persist for the rest of the year?

Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

I think one of the things that we've stated in the past, John, is that movements on currency obviously have a significant impact in general across the Company, depending on where they move. And the best way to really answer that question is really to talk about it on an aggregate move against kind of the world currencies. And as you know, different currencies move in different directions. But, I think a broader-based movement on currencies in the neighborhood of about a 5% level typically has about a top line impact on us of about 3% since 60% of our sales are overseas. And I think that in general, again, if you have movements consistently with currencies in those same ranges at 5%, that typically has about a 1% to 2% impact on our bottom line on average. So, hopefully that kind of gives you an idea. If rates right now are roughly closer to the 131 level in comparison to an upper to mid-kind of 30 level, I think that you're probably looking at maybe 2.5%, maybe 3% on average. If all currencies were kind of moving in that same magnitude, that probably equates to maybe \$0.01 a share per half a year.

John Kreger - William Blair - Analyst

Excellent. Thank you. And then just my follow-up question gets to your comment about seeing an improvement start to play out across different geographies. If you look at that and look at geographies where the markets are typically self-pay, versus markets where they're more government pay, are you seeing a difference in the trajectory of the recovery so far?

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

John, this is Brett. Over 120 countries, it's kind of hard to draw that generalization. So, for instance, countries like Italy which are all self-pay, I think we are starting to see a very slow recovery there as well. Countries where it's all paid by government or largely reimbursed by government, that would include, for instance, the UK and Germany, we're also starting to see some recoveries there. So, I don't know that we've been able to differentiate, based on reimbursement, with that level of definition yet. I think it's more driven by consumer confidence in those regions, and so forth, than anything else. And in countries where there is no reimbursement it's largely driven by employment.

John Kreger - William Blair - Analyst

Okay. Makes sense. And then lastly, do you have a view on the recently passed healthcare reform bill? Do you think it'll have an impact on your business over time?

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Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

Just a few comments on that. The healthcare reform bill largely did not include dentistry. It included some coverage for children up to a multiple of the welfare level, so that would be children under the age of 21. And it also, of course, includes a provision that children up to age 26 now can stay on their parents' coverage. So, those two provisions could in fact result in some expanded procedures for dentistry and, I think, because it's mainly children, it's mainly preventive type procedures rather than heavy reconstructive type procedures. On the other hand, because we are a medical device company, we're subject to the 2.3% excise tax on medical device sales, and that's for class one, class two, and class three medical devices. And most of our products do fall into those categories. So, at this point we see some benefit because of, perhaps, higher coverage for children or dependants up to age 26. And, at least at this point, we're subject to that excise tax and it's a question about how that will affect our pricing and so forth going forward. I think that's not entirely clear yet because the bill hasn't been available for that long and there's going to need to be some changes to the bill, so we're going to have to closely track what happens to that bill before this gets implemented.

John Kreger - William Blair - Analyst

Great. Thanks very much.

Operator

We'll take our next question from Tao Levy with Deutsche Bank.

Tao Levy - Deutsche Bank - Analyst

Great, thank you very much. Two quick questions on the new product you're launching in orthodontics.

Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

Okay.

Tao Levy - Deutsche Bank - Analyst

Is this -- just to be clear, this is just for the front and bottom six, right? Top and bottom six?

Chris Clark - DENTSPLY International Inc. - President & COO

Yes, it's focusing on the minor tooth movement, if you will, of the social six, correct.

Tao Levy - Deutsche Bank - Analyst

And do you have a sense of how many aligners that's going to acquire?

Chris Clark - DENTSPLY International Inc. - President & COO

Yeah, it is a multiple aligner product, Tao, so that could range anywhere from three trays to ten trays, depending on really the specific patient case.



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Tao Levy - Deutsche Bank - Analyst

And then, given that the orthodontic conference is coming up, you made some reference to that market in your prepared remarks. What is your sense of how orthodontics in the market uptick evolves throughout the rest of the year? And anything interesting we could hear out of that conference this weekend? Thank you.

Chris Clark - DENTSPLY International Inc. - President & COO

Yes, I think obviously for us the MTM will be the major thing you'll hear from. I think the the orthodontic case starts, there is no doubt, are down based on all the data we've seen. It is a elective, generally non-reimbursed procedure that certainly can be deferrable. I mean, if your children need braces and you can straighten their teeth at age 14, you can also straighten them at age 17. So it is deferrable. I think the market clearly has seen that. So, in terms of the general orthodontic market, my sense is it will gradually come back, as Brett mentioned. It'll be a gradual recovery. In terms of the specific AO show, my guess is you'll see some, obviously we hope, some excitement on the MTM product.

Tao Levy - Deutsche Bank - Analyst

Great. Thank you very much.

Operator

We'll take our next question from Jeff Johnson with Robert W. Baird.

Jeff Johnson - Robert W. Baird - Analyst

Thank you. Good morning, guys.

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

Good morning, Jeff.

Jeff Johnson - Robert W. Baird - Analyst

Brett, I wanted to start on a couple of maybe bigger-picture organic growth questions. One, I didn't hear you specifically reference implant or ortho organic growth in the quarter. Just can you give us directionality there? And then also, you and I have had some conversations over the last few months about Europe kind of lagging in to the downfall in dental or to the falloff in dental, and probably lagging out, now a good bounce-back this quarter in the European organic growth to plus 2.5%. So, just wondering if anything's changed there? If you're surprised at especially the European bounceback? Any comment there would be helpful.

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

Okay. Sure, Jeff. Implant, ortho, actually endo, all three of our specialties, had low single-digit internal growth during the quarter. Specifically, with orthodontics, our business was much stronger in Europe than it was in the United States. With respect to implants, it was the opposite. Our business was strongest in the United States and weaker outside of the United States. On implant, I think I would add that, even though we had low single-digit growth overall for the world, there were two regions or two countries -- or two regions, frankly, that depressed that number for us, which was CIS and South Korea. And absent CIS and



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South Korea, we would have been mid single-digit internal growth in implant. So, we're still seeing good uptake in that product line. As Chris mentioned, we had our large Symposium in Barcelona in March and we had very strong attendance at that, so that was encouraging. And overall, I think we see the implant market and the orthodontics market both probably experiencing kind of low single-digit growth coming out of the recession here. Again, those grew throughout 2009. Europe was a little bit stronger than we thought it would be in the first quarter, frankly. Your comment -- you're probably recalling what we said on the conference call at the end of the year. We saw very strong growth in the consumable categories in Europe, and I think that is encouraging to us because it's evidence that everyday dentistry's starting to pick up there. Although, with Europe in particular, it's important that we say it varies widely by country. Because we have some countries where their economies are under significant distress right now, and others that seem to be participating in the global recovery.

Jeff Johnson - Robert W. Baird - Analyst

Thanks. That's helpful. And then, on the crown and bridge side, the low single-digit decline there on the prosthetics a much better number this quarter. In some of the patient data we track on a weekly basis, seems like we're seeing a bigger pickup in crown and bridge than we are in a lot of other categories, which is surprising us. Do you think it is end user demand in the US that might be picking up for crown and bridge? Those things only being deferrable for so long? Or do you think there is any restocking going here? I know there was a big destocking impact on your artificial teeth and some of your other prosthetic stuff last year.

Chris Clark - DENTSPLY International Inc. - President & COO

Yes, Jeff, it's Chris. I think, relative to, particularly the US market, my sense is it's rebounding a little bit. I think Brett's comments that we're optimistic that we may be either near the bottom or we can see the bottom from here. Obviously it did decline overall a bit and I do think that, you mentioned it, I think we did have a bit of an easier comp on that business because of the destocking in the prior-year basis.

Jeff Johnson - Robert W. Baird - Analyst

Okay. Thanks. And, last couple of questions, probably just modeling questions, I guess more than anything, for Bill. Acquisition impact the rest of the year with the LOIs that are out there, will that still be kind of in the low single-digit range? Or how should we think about modeling that? And then interest expense. I'm still just not quite clear why it went up sequentially a couple million dollars relative to the last few quarters with interest rates here at the last few quarters having been relatively stable.

Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

Sure. I think you got a couple of different points on that -- on the interest side of the -- well, first up maybe on the acquisition piece. For acquisitions, Jeff, you should -- we only talked really about the acquisitions that we kind of complete, whether we've got an LOI out there or not. So I think your couple tenths of a point, at least at this point, is probably what you should be using in your models until those acquisitions are ultimately completed and/or any other future ones are done. As it relates to the interest expense category, Jeff, there's a couple points associated with that. One is the weakening of the Euro, since that's where all of our cash is. Obviously the interest income is getting translated at a lower level. You've also got the fact that the \$250 million private placement that we completed, that was about \$100 million higher than the one that fell off. And keep in mind that that one is a fixed rate one, which was replacing neither variable debt an/or cash. So, that's probably on average \$750,000 to maybe \$1 million a quarter in that number. Plus, we also had some of the repurchasing activity within this quarter as well.

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Jeff Johnson - Robert W. Baird - Analyst

Alright, so barring any significant Euro moves at this point, the \$5.8 million, somewhere in that ballpark, is a good go-forward number to think about for the rest of the year?

Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

Yes, I think that's reasonable, excluding any additional acquisition or stock repurchase items that are driving that.

Jeff Johnson - Robert W. Baird - Analyst

Okay. And the two deals that have an LOI out there, I know haven't closed so we won't put them in the model, but would they be of any size to note or relatively minor?

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

Jeff, this is Brett. Those are small kind of tuck-under deals. I don't think you need to model those at this point.

Jeff Johnson - Robert W. Baird - Analyst

All right. Thank you, guys.

Operator

We'll take our next question from Adam Poussard with Barclays Capital.

Adam Poussard - Barclays Capital - Analyst

Thanks. Good morning. Can you guys just elaborate on two small acquisitions that you did in Europe? I guess kind of what that added to your capabilities?

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

Yes, the two small acquisitions, one was an endodontics equipment company. So that is kind of a vertical integration. It's a company we did some business with before and we brought that capability in-house. The second is an orthodontic sales and marketing organization in one of the European countries, which we've had a close relationship with for some time, but wanted to acquire to go direct in that country.

Adam Poussard - Barclays Capital - Analyst

Okay. Great. Thanks.

Operator

We'll go next to Derek Leckow with Barrington Research.

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Derek Leckow - *Barrington Research - Analyst*

Thank you. Good morning. Just a couple of follow-ups here on the geographic growth and expectations for Europe. I wanted to kind of quantify your exposure to some of the weaker economies there, especially Spain, Portugal, Greece.

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

What, you're looking for like a percent of sales?

Derek Leckow - *Barrington Research - Analyst*

Yes, I mean, is this something meaningful that we should be concerned about?

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

No -- I mean, obviously probably Spain is the largest of the three. I would say Portugal is a very small component of our European sales. And remember, 40% of our sales are in Europe, and half of that's Germany. The other big countries would be the UK, France, Italy, to a lesser extent the Benelux region. So, the countries that you're mentioning that seem to be under the most pressure, their government's seems to be under the most pressure, are not -- for the most part are not significant countries to our geographic mix in Europe. Spain would be the largest of the three you mentioned.

Derek Leckow - *Barrington Research - Analyst*

All right. And then within that 40% coming from Germany, how's the lab business doing in Germany? And are you getting pretty good visibility on dental visits and so forth? What is your sense for how that economy is doing in those two separate areas? The lab versus the general dental?

Chris Clark - *DENTSPLY International Inc. - President & COO*

Yes, I would say -- it's Chris, Derek. I would say that generally it's probably a bit slower than what we've seen in the US I think there might be a little bit of rebound in terms of procedures in the US I don't know that we've seen anything that significant, per se, over at least a three-month period in Germany that would be noticeably different from where we have been.

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

And what I'd add to that, Derek, is that this general trend we're seeing where the chair-side consumables are rebounding the fastest seems to be applying equally the same in Europe as we see in the United States. So, in kind of the countries you're talking about, we've seen the stuff that's used in the operatory everyday coming back the quickest.

Derek Leckow - *Barrington Research - Analyst*

Okay. Good. And then the rest of world growth that you saw there, the main drivers, I think I missed what you said. But, is that Latin America? Was that where you saw? Is Brazil doing really well? Or what's the --

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Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

We didn't mention what countries, but off the top of my head, the countries that are leading that -- Australia continued to be very strong, Canada was strong, and some of the Latin American countries were strong. So, if I had to summarize those three I'd mention --

Chris Clark - *DENTSPLY International Inc. - President & COO*

Middle East, as well.

Derek Leckow - *Barrington Research - Analyst*

Middle East as well?

Chris Clark - *DENTSPLY International Inc. - President & COO*

Although, that was a pretty deflated base.

Derek Leckow - *Barrington Research - Analyst*

India and China kind of flattish? Is that relative to flat?

Chris Clark - *DENTSPLY International Inc. - President & COO*

India is not growing as fast as we would have expected at this point. I'd say, generally. And that may be a temporary situation, I'm not sure. It's also influenced by South Korea, I mentioned that on the implants, where the economy is quite bad and that I think there is some structural things going on in that market that's slowing things down.

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

I think it's also fair to say, Derek, in that space that, from a comparison perspective, that we also had some easier comps in that category in comparison to last year. So, that number is probably a little bit high in relationship to where we really see it.

Derek Leckow - *Barrington Research - Analyst*

Okay. Okay. Good. And then, just moving on to operating margin, a little bit lighter than we expected. I think you talked about the impact of currency. But, beyond currency, what's driving the increase in spending levels? I think you said there were some one-time true-ups on some bonuses and commissions and stuff like that, but does that roll off in the second quarter? Can you remind me how these increases will play out for the rest of the year?

Bill Jellison - *DENTSPLY International Inc. - Senior Vice President & CFO*

No, I think if you're talking about some of the more variable expense categories?

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Derek Leckow - Barrington Research - Analyst

Yes.

Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

And the impacts. No, I think that it's fair to say, Derek, as you look through really all of last year and from a performance perspective, the impacts of the year were fully reflected, and then I think each one of those quarters, and in fact in some of the periods, were more impacted, especially in the first -- in the middle part. So, I think that all those categories you should expect are going to continue to run at a little bit higher level in comparison to what they did last year, just because of the performance levels that were achieved or expected to be achieved.

Derek Leckow - Barrington Research - Analyst

So it's fair to say we're going to be kind of below the long-term goal of having 30 to 50 basis points of improvement in operating margin this year? Or would you say that it kind of rebound later in the year?

Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

Well, I think, first off, generally we say that on the operating margin side of the equation the guidance and the broader-based assumptions that we give in that category are really more on a multi-year basis. We try not to give specific guidance to that type of number in any of the quarters. However, I would expect, as you saw in the first quarter, improvements at least sequentially on the gross profit margin side, while we were also lower on the SG&A and in the first Q, I think that, as you saw throughout last year, the SG&A rates were coming down. So, some of those comparisons, especially as you get into, let's say, the fourth quarter, would be much more difficult on a comparison and net period. Although, hopefully the reverse of that, with the gross margin side, gross margins in the second half of the year should hopefully look better in comparison to the last year's periods.

Derek Leckow - Barrington Research - Analyst

Okay. So, I think what you're saying, we should kind of be modeling roughly a flattish operating margin for the year?

Bill Jellison - DENTSPLY International Inc. - Senior Vice President & CFO

No, Derek, it's too early. We're not giving operating margins for the year. I think our earnings guidance is probably what you ought to look into it.

Derek Leckow - Barrington Research - Analyst

Yes, I backed into it from the guidance, and I can't seem to get to a number that's flat. So, that's why I'm asking. And then, finally, let me ask a question on the clear aligners. You said you're going to be using your existing lab capacity. And I just wondered if you could elaborate on how much you're going to have to spend in terms of capital spending to grow that business? Or what kind of expectations do you have for initially for the launch and for the spending around that?

Chris Clark - DENTSPLY International Inc. - President & COO

Yeah, it's Chris. Again, the lab we have has a fair amount of capacity. We've obviously geared up and anticipated this and made some investments, really over the previous 12 to 18 months to get ready for it. So, I think we're in pretty good shape today.



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Obviously, if it exceeds our expectations, which is always something to hope for, that's a relatively easy investment for us to make further. I don't think it's a material investment in terms of incremental at this stage in the game.

Derek Leckow - *Barrington Research - Analyst*

And then just strategically, does this, perhaps, cannibalize any of your existing orthodontic products? Or does it compete in any way anything that you currently sell in certain terms of your clear self-ligating brackets and so forth?

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

I think it's really largely a different segment. We do offer a chair-side MTM basis product that has done relatively well for us, but this now expands that into a lab-based service. Again, I think that most of this would be incremental to us, as opposed to cannibalizing our bracket sales.

Derek Leckow - *Barrington Research - Analyst*

But, at least as it relates to that chair-side MTM product, that should be something we would expect most practitioners will probably just opt to use your lab. Is that fair to say?

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

My guess is, Derek, it's probably going to be largely incremental. The folks that are doing it chair-side probably are doing it because they like to do it themselves. And again, we'll still offer that. But, if they don't want to do it themselves, we didn't have an offering previously and now we do. And obviously some other folks do and that's now a segment we think is pretty attractive and we're pretty excited about our entry into it.

Derek Leckow - *Barrington Research - Analyst*

Alright, very good. Thanks a lot. Good luck.

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

Thanks, Derek.

Operator

We'll go next to Brian Delaney of EnTrust.

Brian Delaney - *EnTrust - Analyst*

Hi, guys. On the clear liner product as well, have you guys thought about price points? Where should we think the price point for this is? And second question is, you said it's for minor tooth movement. Is that the ultimate goal? Or do we want to see how it works first, and then is there opportunities to get into bigger type of offerings?

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Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

Yes, let me answer the second one first. I mean, we believe it is a minor tooth movement product. I think that's what the technology at this point delivers and what we're comfortable with. Again, I think there's a demonstrable need for that product, and I think we're very comfortable with how that's positioned. I wouldn't necessarily say, "Hey, you can't migrate over time." But, that's certainly not the going-in strategy. I think, to a degree, it is what it is. And we're excited about it. The second piece, in terms of pricing, I hesitate to give specific pricing as we're not in the market yet. But, what I guess I would leave you with is it's going to be pretty competitively priced. So, from that angle we think we offer a good value equation to the customer, and obviously we're excited about the margins on our end, as well.

Brian Delaney - *EnTrust - Analyst*

Great. Thank you.

Operator

We'll take our next question from Scott Green with Bank of America Merrill Lynch.

Scott Green - *Bank of America Merrill Lynch - Analyst*

Hi. Thanks for the question. Question on a new product in endo. Your new skinny nickel titanium rotary path files are first to market and I was wondering if you could talk about initial consumer adoption trends and whether you think it can drive market share gains that spill over into the larger nickel titanium product line that makes up a bigger piece of the endo pie? I'm not sure why dentists would need multiple vendors there.

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

Scott, let me take a stab at that. The path file is kind of a unique file that a dentist or endodontist can use at the beginning of the procedure to kind of find their way to the apex of the tooth. It's an important tool for them to use. Obviously, we try to do dual branding and packaging solutions and so forth with our other files -- with that file to grab more market share. I would say that probably the path file doesn't provide a unique link to our other branded products, though. The path file could be used with the competitors' file as well. So, we came out with that file just because we saw that there was a need for a clinical solution to that issue. And we're happy with the success of that file, and of course we're going to use it to our advantage to the extent that we can. But, I would say that it's not -- there's not a technical link between that and the other files at this point.

Bill Jellison - *DENTSPLY International Inc. - Senior Vice President & CFO*

Yes, I view it as an adjunct to our existing line.

Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

Yes.

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Scott Green - Bank of America Merrill Lynch - Analyst

Okay. And then you've talked about last year distributor inventory destocking and a little update here. I was wondering where we stand in terms of inventory days out there and the channel before the recession, versus today, and whether you expect or have seen any restocking? Or maybe that this new level is the new normal going forward?

Chris Clark - DENTSPLY International Inc. - President & COO

Yes, I guess -- it's Chris. I guess I would say that in the quarter we really didn't see any significant net change either way. Obviously, in the prior year base we did see some destocking and we commented, I think, in a few cases in terms of where that might have given us a bit of favorable comparisons. In terms of is this the new norm, my gut reaction is that demand will need to come back reasonably -- in a reasonably healthy manner for customers to look at it and say they need more inventory to service. I think in all likelihood, they're doing an effective job servicing with the inventories they have, being this the new level. Might there be some pockets in terms of stocking? Yes, there may be. But, I don't know that I see a wholesale change, if you will, in terms of the inventory levels as the economy recovers, per se.

Scott Green - Bank of America Merrill Lynch - Analyst

Okay. And then one question on the implant line. I believe you expanded the North American implant sales force here at the beginning of the year. Was that driven by better visibility into market trends or more confidence into your new model ANKYLOS or other factors?

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

Well, we made a couple of investments in sales and marketing, kind of is more last year than this year. Specifically with respect to the North American market, that's a market we've been investing in for a couple of years here, both in sales, resources, and marketing resources. We do believe that that ANKYLOS product line is a strong compliment to our XiVE product line. We've got two strong brands here in the United States, and they've been growing above market here for two or three years in a row and I think that continued in the first quarter where we had double-digit growth in implants in the US So, obviously we're trying to back the brands we think were the strongest around the world, but that's an area where we've had kind of consistent investment for some time now.

Scott Green - Bank of America Merrill Lynch - Analyst

Okay. Great, thank you.

Bret Wise - DENTSPLY International Inc. - Chairman & CEO

Thank you.

Operator

This does conclude our question-and-answer session. I'd like to turn the conference back over to our speakers for any additional or closing remarks.

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Bret Wise - *DENTSPLY International Inc. - Chairman & CEO*

Okay. Thank you, Christian. Thank you all for attending this morning. I'd say that we're encouraged by the early signs of growth in our markets and we look forward to updating you on our progress as we move throughout the year. Thank you.

Operator

This does conclude today's conference. Thank you for your participation.

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